Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Qwest Communications International Inc.	)	**WC Docket No. 02-314**
	)	
Consolidated Application for Authority to Provide In-Region, InterLATA Services in Colorado, Idaho, Iowa, Montana, Nebraska, North Dakota, Utah, Washington and Wyoming	)	

REPLY DECLARATION OF JERROLD L. THOMPSON AND THOMAS R. FREEBERG

Cost-Based Rates for Unbundled Network Elements and Interconnection

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TABLE OF EXHIBITS

Exhibit	Description
Reply Exh. JLT/TRF-1	Matrix Showing Qwest's Responses in Prior Proceedings to Parties' Arguments Raised Once Again in This Proceeding

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Pursuant to 47 C.F.R. § 1.16, Jerrold L. Thompson and Thomas R. Freeberg declare as follows:

1. My name is Jerrold L. Thompson. I submitted declarations with Qwest's Applications in WC Docket Nos. 02-148 and 02-189 showing that, in each of the states that are the subject of the Application, Qwest's rates for UNEs, interconnection, and collocation comply with Sections 251, 252, and 271 of the Act and with the FCC's rules. This Reply Declaration refutes the arguments to the contrary submitted by AT&T, Covad, Integra, the Montana PSC, One Eighty, the Payphone Associations, and WorldCom. I am primarily responsible for paragraphs 3-28 of this declaration and the Exhibit hereto.

2. My name is Thomas R. Freeberg. I submitted declarations with Qwest's Applications in WC Docket Nos. 02-148 and 02-189 showing that, in each of the states that are the subject of the Application, Qwest's offerings of local interconnection service ("LIS") trunks fully satisfy Section 251(c)(2) of the Act and Checklist Item One of Section 271(c)(2)(B)(i). This Reply Declaration refutes the arguments to the contrary submitted by Level 3. I am primarily responsible for paragraphs 29-32 of this declaration.

I. INTRODUCTION AND EXECUTIVE SUMMARY

3. For the most part, the opposing parties' comments on Qwest's UNE and interconnection rates simply recycle the arguments that they made – and that Qwest already has refuted – in previous phases of this process. Indeed, some of them (*e.g.*, WorldCom and the Payphone Associations) merely incorporate by reference their submissions in the prior dockets .[1/] Accordingly, we hereby incorporate by reference the portions of our previous declarations containing responses to these arguments. [2/] Those previous declarations also respond to the

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1/ WorldCom *Qwest III* Comments at 25-26; Payphone Associations *Qwest III* Comments at 1; *see generally* Reply Exh. JLT/TRF-1. The Payphone Associations have now raised identical arguments in an informal complaint filed against Qwest on Oct. 8, 2002, and attached to their comments; the issues should be addressed in the context of that informal complaint proceeding, not in this Section 271 proceeding.

2/ *See generally Qwest I* Reply Brief; *Qwest II* Reply Brief; Reply Declaration of Jerrold Thompson, 'Cost-Based Rates for Unbundled Network Elements and Interconnection', *Qwest I* at Tab 8 ("*Qwest I* Thompson Reply Decl.") Reply Declaration of Jerrold Thompson, 'Cost-Based Rates for Unbundled Network Elements and Interconnection', *Qwest II* at Tab 8 ("*Qwest II* Thompson Reply majority of AT&T's arguments, which, despite its lengthy filing and revised declarations, are largely a replay of the arguments AT&T already presented. Reply Exhibit JLT/TRF-1 to this declaration is a table listing opposing parties' arguments in this proceeding and specific page references to our responses to those arguments in the *Qwest I* and *Qwest II* dockets.

4. The arguments that AT&T and other parties seek to replay here are no more availing than they were when Qwest responded to them in full the first time they were made. Although Qwest has now responded to AT&T's and other parties' arguments, in most cases, AT&T and the other opposing parties simply ignore the responses provided by Qwest, and instead merely recycle their prior arguments. Thus, for example, AT&T repeats its unfounded allegation that Qwest might somehow spy on CLECs' use of electronic database tools to determine the zone in which prospective customers are located, and use that information to thwart entry [3] – notwithstanding Qwest's demonstration that such spying is simply not

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Decl."); Reply Declaration of Thomas Freeberg, 'Interconnection & Reciprocal Compensation, *Qwest I* at Tab 1 ("*Qwest I* Freeberg Reply Decl."); Reply Declaration of Thomas Freeberg, 'Interconnection & Reciprocal Compensation, *Qwest II* at Tab 1 ("*Qwest II* Freeberg-Reply Decl.")

[3] AT&T *Qwest III* Comments at 79-80 n.280. *Compare* AT&T Michael Lieberman and Brian Pitkin Declaration ("AT&T Lieberman/Pitkin *Qwest III* Decl."), *Qwest III*, Tab L at ¶ 49 ("because Qwest will know exactly where CLECs intend to enter – indeed, CLECs must request customer UNE zone information directly from Qwest – Qwest has a competitive advantage that will allow it to thwart competitive entry") *with id.* n.23 ("The only precise method currently available to CLECs [to determine the zones in which each customer falls] (documented on Qwest's website . . .) is to enter each customer it plans on targeting into Qwest's IMA database.").

possible. 4/ Nor do the opposing parties' comments reflect other critical developments since earlier phases of these proceedings. For example, AT&T for some reason continues to argue for the application of the benchmark methodology separately to local switching and to transport/tandem switching. 5/ But as AT&T must recognize, this issue is moot, because Qwest has recently agreed to recalculate its rates based on the separate benchmark methodology AT&T favors. 6/

5. This declaration focuses on responding to the four arguments, out of the myriad of recycled arguments, that appear to raise new points to which Qwest has not already responded. First, we show that there is no merit to AT&T's new twist on an argument that it made previously relating to the network operations input used in setting Qwest's loop rate in Colorado. Second, we show that AT&T's new twist on its challenge to the CPUC's decision to use the default HAI model methodology for determining loop cable routes, rather than the so-called

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4/ *Qwest II* Thompson Reply Decl. at ¶¶ 55-56.

5/ AT&T *Qwest III* Comments at 76-77; AT&T Lieberman/Pitkin *Qwest III* Decl. at ¶¶ 14-20.

6/ *See Qwest III ex parte* letter from David L. Sieradzki to the Secretary, FCC, [rate reduction revisions] (Oct. 7, 2002) ("*Qwest Oct. 7 Ex Parte*"). Qwest filed revised SGAT Exhibit A's incorporating the reduced rates with the regulatory agencies in all eight states affected by this adjustment during October 16-18, 2002. Copies of these documents will be submitted in the record of this proceeding in the near future.

Although AT&T continues to calculate its benchmarking using state-specific adjusted dial equipment minutes of use, this Commission's standard minute-of-use assumptions are appropriately applied here for reasons that Qwest has explained before. *See New Jersey 271 Order,* ¶ 53; *Qwest II* Thompson Reply Decl. at ¶¶ 11-15.

"Minimum Spanning Tree" module, is no more availing than AT&T's previous arguments on this point. Third, we demonstrate that there is no connection between the Montana PSC's demand that Qwest initiate a "full revenue requirements and rate design" retail rate case and the PSC's purported concern that Qwest's intrastate access charges may cause a "price squeeze," and that, in any event, it would be an "abuse of the Section 271 process" to address this issue in this proceeding, as dissenting Montana PSC Commissioner Bob Rowe explained (consistent with prior FCC precedent). Fourth, we demonstrate that Level 3 is wrong in contending that Internet-bound traffic should be treated as local traffic for purposes of measuring relative use for billing interconnection trunks, and that, in any event, the Commission has held on numerous occasions that disputes relating to the treatment of Internet-bound traffic are not to be addressed in the context of Section 271 proceedings.

II. QWEST'S COLORADO UNBUNDLED LOOP RATES COMPLY WITH TELRIC

A. The CPUC's Treatment of Network Operations Expenses Was Reasonable and Did Not Produce a Higher Recovery Than Qwest Had Proposed.

6. AT&T asserts that it "only recently discovered" what it calls "an additional TELRIC error" relating to the CPUC's decision to apply a 4% downward adjustment to the network operations expense factor used in the HAI model (affecting Qwest's Colorado loop rates), and the CPUC's decision to reject AT&T's proposed 50% downward adjustment (consistent with decisions by regulatory

agencies in Arizona, Minnesota, and other Qwest states rejecting the same proposal). [7/] The "recent" nature of AT&T's "discovery" is not attributable to any new facts or laws, but to AT&T's "second wind" in ginning up arguments to prolong consideration if not obtain rejection of this application. In any event, the discovery does not appear to be recent, but is essentially the same network operations expense argument that it made in the previous Qwest 271 proceedings but in different form. In all events, that argument is without merit for the reasons expressed in the Thompson *Qwest I* Reply Declaration, [8/] and as set forth below.

7. As a preliminary matter, AT&T never presented to the CPUC its latest spin on the network operations expense argument, despite ample opportunities to do so over the course of a cost docket spanning more than a year and a half. Nor did it present that point to this Commission during the *Qwest I* or *Qwest II* proceedings. It is improper for AT&T to present this new argument without having afforded the state commission an opportunity to consider it. As a general practice, the Commission does not consider arguments -- particularly fact-intensive pricing arguments -- that a party fails to raise in the underlying state pricing proceeding and then raises for the first time in a Section 271 proceeding. [9/] Application of this rule is particularly appropriate here, where any meaningful

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7/ AT&T *Qwest III Comments* at 71; *see also* AT&T Douglas Denney Declaration, Qwest III, Tab K ("AT&T *Qwest III* Denney Decl."), *passim*.

8/ *Qwest I* Thompson Reply Decl. at ¶¶ 64-68.

9/ *See*, *e.g.*, *BellSouth 5-State 271 Order*, at ¶¶ 31, 78 and n.239; *Vermont 271 Order*, at ¶ 20.

analysis of AT&T's arguments would require a close reading of the manner in which two different cost models treated one particular expense factor, the parties' proposals for the use and amendment of that factor in their own and one another's models, and the CPUC's specific analysis and decision concerning that lone input. Accordingly, "AT&T's arguments on this point present a textbook illustration of why this Commission rejects efforts by opponents of a section 271 application to raise arguments that they deprived the relevant state commission of a full opportunity to consider." [10]

8. Ironically, while the specific twist AT&T seeks to give to its argument concerning network operations expenses may be "newly discovered," AT&T has already made a very similar argument to the CPUC, which squarely rejected it. In the *Qwest I* proceeding, AT&T sought to relitigate that CPUC-rejected argument before this Commission, contending that Qwest's network operations expense factor should have been reduced by 50% to reflect alleged forward-looking efficiencies, rather than by 4%, as the CPUC ordered. [11] Qwest responded by showing that the CPUC's decision was appropriate and well-supported, and that AT&T's proposal to reduce the network operations factor was unjustified because, among other things, it rested on unsupported speculation,

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10/ *Qwest I* Thompson Reply Decl., ¶ 67.

11/ AT&T *Qwest I* Declaration of Dean Fassett and Robert Mercer, Tab F ("AT&T Qwest I Fassett/Mercer Decl.") at ¶¶ 24, 59-65.

never presented on the record to the CPUC, about possible ways in which efficient carriers might supposedly try to reduce expenses. [12]/

9. The one "new twist" that AT&T now presents is the allegation that the CPUC adopted a network operations expense "dollar additive that is nearly double the additive advocated by Qwest." [13]/ But AT&T's argument is not only new – and therefore waived – but also erroneous and highly misleading. As an initial matter, AT&T's argument is misleading because it focuses only on one narrow factor, rather than examining the totality of expense factors. Based on the allegation (which, as I show below, is incorrect) that the CPUC adopted an excessive network expense figure, AT&T wrongly implies that the CPUC-adopted loop rates recover expense costs substantially higher than those proposed by Qwest. In fact, however, the Colorado loop rates recover substantially *lower* expense costs than those proposed by Qwest and appropriate for an efficient carrier. Indeed, the CPUC-ordered figures aggressively assume that an efficient carrier could operate at a level of operating expenses a *full 66% lower* than what Qwest actually incurs. [14]/

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[12]/ *Qwest I* Thompson Reply Decl. at ¶¶ 64-68.

[13]/ AT&T *Qwest III* Denney Decl. at ¶ 10.

[14]/ AT&T chooses to dispute one of the few issues on which the CPUC largely agreed with Qwest's position, but ignores the numerous issues on which the CPUC disallowed expenses that Qwest actually incurred and that a reasonably efficient carrier would necessarily incur. The CPUC adopted indirect expense cost factors that were $3.31 per loop *lower* than what Qwest had proposed (although $2.96 higher than what AT&T had advocated). The network operations expense factor is only one of five different non-tax expense factor categories that are added on to the direct investment-related costs in computing the total TELRIC cost of UNEs; the other four factors are maintenance expense, general support, variable overheads,

10. Moreover, AT&T is wrong in claiming that the network expenses adopted by the CPUC are too high or, specifically, that they are higher than what Qwest proposed. They in fact are 4% lower than what Qwest witnesses proposed the CPUC use if it were to adopt the HAI model. AT&T's argument to the contrary improperly mixes and matches the network expense factor used in Qwest's TELRIC loop cost model with the supposedly corresponding input in the entirely different HAI cost model. Qwest's model in the CPUC cost docket treated network operations expenses as a percentage factor that is applied to direct investment amounts; the resulting total network expenses to be included in the TELRIC rates thus vary based on the level of investment. By contrast, AT&T's HAI model treats network operations expense as a flat dollar amount per loop. Because of the different ways the two models treat these network operations expenses, Qwest's approach to them necessarily varied with the model at issue. [15]/

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and commercial (carrier-to-carrier) marketing costs. In Qwest's TELRIC loop model analysis, Qwest's proposed loop cost per line included a total of $11.13 in expense costs per line. The equivalent costs as advocated by AT&T were $4.91. For operating expenses in total, the CPUC adopted rates that included expense costs of $7.87 – $2.96 higher than AT&T's proposal and $3.31 lower than Qwest's proposal. This amount equates to allowing Qwest recovery of only 34% of the actual expenses (excluding depreciation and taxes) that it incurred to provide service in Colorado during 2000, despite the lack of any showing that an efficient carrier would be able to avoid such a substantial proportion of expenses. Thus, once again, AT&T ignores the fact that "TELRIC is not a single rate but a ratemaking methodology that may yield a rather broad range of rates." [*WorldCom, Inc. v. FCC*, No. 01-1198 (D.C. Cir. Oct. 22, 2002)

[15]/ In the context of the Qwest model, Qwest started with 100% of the network operating expense it actually incurred during 2000. This amount was adjusted by a net productivity factor to be forward looking. The network operating expenses were then divided into four categories of costs: power usage, subscriber line testing,

11. The CPUC ultimately adopted loop rates based on the HAI model. To assess network expenses in the HAI model, AT&T had proposed starting with Qwest's adjusted year 2000 network operations expenses, and arbitrarily reducing this amount by 50%, purportedly to reflect the efficiencies that AT&T contended an efficient carrier would experience on a forward-looking basis (although AT&T presented no facts to support its speculations in this regard). This figure, when divided by the total number of lines, produced network operations expenses of $1.22 per loop. [16] Qwest opposed AT&T's proposed 50% across-the-board reduction to network operating expenses, and offered adjustments to the HAI model to eliminate this reduction. Qwest demonstrated that, given Qwest's

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interoffice testing and other network operating expenses. The other network operating costs (those excluding testing and power usage) were used to develop a loading factor of 7.296 percent of direct costs. This factor was applied to the direct costs for all the elements contained in the Qwest model, including loops. The power and testing components of net operating expenses are used to develop factors that are added to the maintenance factors for various accounts. This assignment of power and testing costs is designed to track cost causation principles. For instance, the power usage factor is applied to electronic equipment but not cable because it is the electronic equipment such as switching that uses the power. In developing these testing and power factors Qwest again started with the actual expenses it incurred during 2000 and conducted a similar process to develop cost factors to apply to direct investment cost categories.

AT&T alleges that Qwest proposed a $1.87 "loop additive" for network operations and other expenses. *See* AT&T Denney *Qwest III* Decl., ¶ 10 (Matrix, col. (1), row "Total"). But Qwest never proposed any such amount as a specific cost figure to use in calculating loop rates. Rather, the figure submitted by Mr. Denney appears to be simply the result of applying the various expense factors (or portions thereof) to the loop investment within Qwest's model. The number appears nowhere in Qwest's model.

[16] AT&T *Qwest III* Denney Decl., ¶ 6.

extensive program of investing in and improving its network operations, the efficiencies of a modern network were already reflected in the current cost and there was no basis for reducing expenses further. Thus, in the context of the HAI model, Qwest advocated a network operations expense cost of approximately $2.70 per loop.

12. The CPUC carefully considered the parties' proposals, concluding that "no support exists for an additional reduction" AT&T had proposed. [17] The CPUC did, however, believe a 4% adjustment was appropriate to reflect anticipated productivity improvements offset by inflation, and related forward-looking changes. It therefore adopted loop rates that incorporated Qwest's proposed network operations expenses for the HAI model, reduced by 4%, to produce a cost of $2.60 per loop, on a statewide average basis. Neither AT&T nor any other party sought reconsideration of this aspect of the CPUC decision. [18]

17/ *Colorado Pricing Order, Qwest I*, Att. 5, App. I at 62. The CPUC explained, "We do not agree with the Joint Intervenors that a TELRIC carrier's Network Operations Expenses would be 50% less than the cost used by Qwest. We do not believe that the Joint Intervenors have adequately supported the HAI Model's default deflator of 50%. However, we do agree that there should be some degree of recognition that the utilization of forward-looking technologies will likely reduce future Network Operations Expense. Therefore, we will adjust this expense by the net of the productivity/inflation factor of 4% discussed *infra*." *Id.* at 63.

Notably, the 4% adjustment adopted by the CPUC already fully accounts for the allegations that network operations expenses would need to be adjusted to account for functions recovered through NRCs or collocation charges. AT&T *Qwest III* Denney Decl., ¶ 8.

18/ *See, e.g.,* Application of AT&T Communications of the Mountain States, Inc., and XO Colorado, Inc. for Re-hearing, Re-Argument, and Reconsideration, *Qwest I*, Att. 5, App. I, Vol. 3 at Tab 412.

Indeed, every state commission in Qwest's region that has considered AT&T's argument for a 50% across-the-board reduction in network operating expense costs has rejected it, even including the Minnesota PUC and the Arizona Corporation Commission. [19]

13. AT&T's analysis is independently undermined by a number of other discrete errors. For example, AT&T's assertion that Qwest effectively supported a network operations expense factor 23.6% lower than it actually advocated is a gross fabrication. [20] Similarly, AT&T now argues that its proposed 50% reduction was justified based on data that the CPUC did not consider – and could not possibly have considered. AT&T's argument rests on purported trends

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[19] Even the Arizona and Minnesota commissions, which set the lowest UNE rates in the Qwest region, if not the country, could not accept AT&T's proposed 50% network operations expense adjustment, and instead both agencies adopted 15% adjustments. *See Investigation into Qwest Corp.'s Compliance with Certain Wholesale Pricing Requirements for Unbundled Network Elements and Resale Discounts*, Docket No. T-00000A-00-0194, Decision No. 64922, Phase II Opinion and Order (Ariz. Corp. Comm'n June 12, 2002) at 26-27; *Commission Review and Investigation of Qwest's Unbundled Network Elements Prices*, Docket Nos. P-421/CI-01-1375, *et al.*, Order Setting Prices and Establishing Procedural Schedule (Minn. Pub. Util. Comm'n Oct. 2, 2002) (available at http://www.puc.state.mn.us/docs/orders/02-0134.pdf), Attachment at A-2.

[20] AT&T unjustifiably adjusts the network operations expense factor that Qwest proposed for use in its own model downward by 23.6%, reflecting the difference between the $23.55 loop rate produced by Qwest's model and the $18.00 loop rate that the CPUC adopted during the prior "331T" proceeding and that Qwest stated should be retained. AT&T *Qwest III* Denney Decl. ¶ 10 n.8. But Qwest never advocated this approach or suggested that its network expenses from the 2001 "577T" proceeding should be applied in any manner to the $18.00 loop rate from the "331T" proceeding.

through 2001, [21]/ but no data from 2001 were available to the CPUC because the cost proceeding was conducted during calendar year 2001. The FCC has repeatedly rejected arguments that a state commission's TELRIC analysis was wrong because it failed to take into account subsequent developments after the close of the record in the state proceedings. [22]/ Moreover, AT&T's contentions about trends in network operations expense reductions since 1996 are misleading, since they ignore the unusually high network operations expenditures that U S WEST incurred during 1994-96 to restructure and centralize its engineering functions, making them much more efficient and saving substantial network costs in the longer run. [23]/

14. In sum, there is no basis for AT&T's contention that that a forward-looking network operations expense factor should be 50% lower than the actual amounts incurred by Qwest. The CPUC, like every other state commission considering the issue in Qwest's region, properly rejected that contention, and there is no justification for re-examining it here.

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[21]/ *Id.*, ¶ 7.

[22]/ *See*, *e.g.*, *WorldCom, Inc. v. FCC*, 2002 WL 31360443, * 5 (D.C. Cir. Oct. 22, 2002) (upholding *Massachusetts 271 Order* on this point); *AT&T Corp. v. FCC*, 220 F.3d 607, 617 (D.C. Cir. 2000) (upholding *New York 271 Order* on this point); *Vermont 271 Order*, at ¶ 23.

[23]/ *See* Prefiled Rebuttal Testimony of D.M. (Marti) Gude, Docket No. 99A-577T (July 20, 2001), pp.17-18*Qwest I*, Att. 5, App. I, Vol. 3 at Tab 228.

B. The CPUC Reasonably Declined To Use the "Minimum Spanning Tree" Cable Routing Option in the HAI Model

15. On a separate issue also affecting Colorado loop pricing, AT&T recycles its old opposition to the CPUC's well-supported decision to not to use the HAI Model's "Minimum Spanning Tree" algorithm. [24] The CPUC chose instead to use the default cable routing algorithm, rejecting the use of the MST module because:

> The customer placement based on MST is not representative of the real world considerations that are properly taken into account in a TELRIC study. . . . TELRIC does not require ignoring other real world limitations or sources of network placement cost such as buildings, rivers, lakes, etc. Therefore, the MST results in drop lengths that are too short [and] will result in consistent undercompensation to Qwest . . . ." [25]

16. Qwest has addressed the invalidity of the MST function before. Although AT&T refers to the algorithm as the "strand distance normalization ('SDN') option" [26] rather than the MST algorithm – the term used consistently both in the CPUC proceedings and in *Qwest I* and *Qwest II* –both terms refer to the same optional function in the HAI model.

17. In a new twist that was never presented to the CPUC, and until now has never been presented to the FCC, [27] AT&T now argues that the CPUC's

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[24] AT&T *Qwest III* Fassett/Mercer Decl. at ¶¶ 65-72.

[25] *Colorado Pricing Order* at 42; *see also* Thompson *Qwest I* Reply Decl., at ¶¶ 55-59.

[26] AT&T *Qwest III* Fassett/Mercer Decl. at ¶ 66.

[27] *See supra* paragraph 6 and accompanying footnotes.

decision not to use the MST algorithm distorts the distribution of Colorado wire centers to the zones used for rate deaveraging. [28/] But this argument is circular: AT&T believes the effect on the wire center distribution is distorted because it believes the proper rates are those that use of the MST algorithm would have produced. Its entire argument fails if the latter premise is rejected, as it should be, for the reasons discussed in the Thompson *Qwest I* Reply Declaration. [29/] Any change in cost modeling methodology would have an impact on the cost-based allocation of wire centers to zones. But the fact that the allocation generated by the standard version of the HAI Model differs from that generated using the MST/SDN module does not mean that the former is not a reasonable and TELRIC-compliant choice for a state commission to have made. In any event, the CPUC has already made it clear that its allocation of wire centers to zones will be one of the major issues to be re-examined during the upcoming phase of its UNE pricing proceeding. [30/] There is no reason for the FCC to second-guess the CPUC on this point.

28/ AT&T *Qwest III* Fassett/Mercer Decl. at ¶¶ 65-72.

29/ *Qwest I* Thompson Reply Decl. at ¶¶ 55-59

30/ *Colorado Pricing Further Reconsideration Order*, *Qwest I*, Att. 5, App. I, Vol. 2, Tab 636, at 12-15.

III. QWEST'S ACCESS CHARGES AND UNE RATES DO NOT CREATE A "PRICE SQUEEZE."

A. The Montana PSC's Intrastate Access Charge/Price Squeeze Objections Are An "Abuse of the Section 271 Process."

18. In its *Qwest II* evaluation, the Montana PSC expressed concern that Qwest's intrastate access rates could create a "price squeeze" in the provision of intrastate long-distance services. On that basis, the Montana PSC stated that it could not recommend Qwest's Montana application to be in the public interest unless Qwest initiated, by October 1, 2002, a "full revenue requirements and rate design case."31/ In response, Qwest filed a letter with the PSC proposing to open a generic rulemaking on Qwest's and other carriers' access charges and the possible need for rate rebalancing. 32/ The Montana PSC now states that, because Qwest did not comply with its condition, "Qwest's interLATA entry in Montana is not in the public interest." 33/

19. With all due respect, the Montana PSC's concerns are unfounded and are, in any event, irrelevant to the merits of this application. In the words of dissenting Montana PSC Commissioner Bob Rowe, former chairperson of the NARUC Communications Committee, "[t]he Montana Commission's action is an

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31/ *Qwest II* Montana PSC Evaluation at 7, 9-10, 57.

32/ *See* Letter from Rick Hays, Qwest Vice President-Montana, to Chairman Gary Feland, Montana PSC (Oct. 1, 2002) ("*Hays Letter*"), included as Attachment 3 to *Qwest III ex parte* letter from David Sieradzki to the Secretary, FCC [updating information provided in 10/7 *ex parte*], (Oct. 11, 2002).

33/ *Qwest III* Montana PSC Evaluation at 3.

abuse of the Section 271 process . . . ." [34] Commissioner Rowe's analysis is cogent and instructive:

> I respectfully but strongly disagree with one portion of the Montana Commission's recommendation. The FCC should decline the Montana Commission's invitation to address intrastate revenue requirements, rate design, and access rates under the umbrella of the public interest review. This is an important tangle of closely related issues, but a knot that the Montana Commission should cut through itself, using the statutory tools it already possesses, rather than borrowing the federal hedge clippers.
>
> While the Act is concerned with opening all markets to competition, the primary focus of Section 271 is opening the local market, at which time the Regional Bell Operating Company may enter the long distance market. The many detailed requirements imposed under Section 271 focus on the local market. . . . . There is no similar nexus between intrastate long distance rates and any specific element of Section 271. I am aware of no case in which the FCC has conditioned Section 271 approval on reduction of intra-state access rates.
>
> The Montana Commission's position is based primarily upon an alleged price squeeze in the intraLATA long distance market. . . . The FCC has recognized the complexity of the wholesale/retail price squeeze issue, and appears to be moving with appropriate caution, and with sensitivity to the Section 2(b) reservation to the states of authority over intrastate rates. There is similar complexity associated with any access/long distance price squeeze, but there is no similar nexus between the alleged price squeeze and the elements of Section 271 review. Further, the Montana Commission's proffered remedy, which it requests the FCC require under its Section 271 public interest review, is a complete revenue requirements and retail rate design case concerning regulated intrastate services. This second full leap away from Section 271 does not (for FCC purposes) directly relate to the alleged access/long distance price squeeze, and invites an even greater FCC engagement in complex intrastate ratemaking. *This is a well-intentioned bad idea.* Again, this is a timely and important set of

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[34] *Id.* at 5 (Separate Statement and Dissent of Commissioner Rowe).

issues, but a set of issues that should be addressed by the Montana Commission under its own authority. [35]/

20. As Commissioner Rowe points out, there is no nexus between intrastate access rates and the critical "public interest" issue implicated by Section 271 – the openness of the *local* market. Indeed, the FCC has held that completion of access charge reform is *not* a prerequisite to Section 271 approval, and that there should be no link between Section 271 approval and access charge reform. [36]/ Moreover, on the merits, the FCC has made clear, and the Eighth Circuit has agreed, that section 272(e) and other structural safeguards are more than adequate to protect against any threat of a "long-distance price squeeze."[37] Finally, even

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[35]/ *Qwest II* Montana PSC Evaluation at 60-62 (Separate Statement of Commissioner Rowe) (emphasis in original).

[36]/ *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, Supplemental Order Clarification, 15 FCC Rcd 9587, 9598 ¶ 19 (2000) ("*Supplemental Order Clarification*") ("Congress anticipated that some [BOCs] would obtain authorization under 47 U.S.C. 271 to originate in-region long-distance services before the completion of access charge reform."); *Qwest II* Brief at 191-92.

[37] *Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended*, 11 FCC Rcd 21905, ¶ 13 (1996) ("[t]he structural and nondiscrimination safeguards contained in section 272 ensure that competitors of the BOC's section 272 affiliate have access to essential inputs . . . on terms that do not discriminate against the competitors and in favor of the BOC's affiliate"); *Supplemental Order Clarification*, ¶ 20 (Section 272 requirements "provide adequate safeguards against any effort by an incumbent to obtain an unfair competitive advantage in the long-distance market by discriminating against unaffiliated IXCs or by improperly allocating costs or assets between itself and its long-distance affiliate"); *Access Charge Reform,* First Report and Order, 12 FCC Rcd 15982 ¶ 279 (1997) ("independent (non-BOC) incumbent LECs have been providing in-region, interexchange services on a separated basis" for over ten years "with no substantiated complaints of a price squeeze."), *aff'd*, *Southwestern Bell Tel. Co. v.*

apart from that precedent, any FCC decision to withhold section 271 relief on the ground that a given state had failed to reform intrastate access charges and other rates would squarely violate Congress's injunction against "extend[ing] the terms used in the competitive checklist,"47 U.S.C. § 271(d)(4), which omits any such requirement. For all these reasons, it would be improper for the FCC to consider this issue here. [38]/

21. A "full revenue requirements and rate design case," as sought by the Montana PSC, would address far more than the level of intrastate access charges – it would involve a complete new determination of Qwest's costs, rate structures, and rate levels for all intrastate regulated services. Thus, even if it were proper (which it is not) to link Section 271 approval to the mitigation of an alleged price squeeze induced by intrastate access charges, the "full revenue requirements and rate design case" requested by the Montana PSC would hardly be a properly targeted remedy to that purported problem. Indeed, the alternative suggested by Qwest – an industry-wide, collaborative rulemaking proceeding on access rate

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FCC, 153 F.3d 523, 548 (8th Cir. 1998) (specifically upholding FCC on this point and rejecting long-distance price squeeze concerns).

[38]/ It is also notable that the Act specifically prohibits use of a "rate-of-return or other rate-based proceeding" – *i.e.*, a "full revenue requirements and rate design case" – for UNE ratemaking. 47 U.S.C. § 252(d)(1)(A)(i). In light of the prohibition of conventional rate cases in this closely related context, it unimaginable that Congress would have intended that such a rate case be imposed as a prerequisite for Section 271 approval.

rebalancing and intercarrier compensation [39]/ – would more narrowly, but more directly and far more effectively, address the alleged price squeeze.

22. In addition, as the Montana Consumer Counsel points out, there is no intrastate access charge-induced price squeeze in Montana, because Montana law and the PSC's rules require a standard imputation test in which Qwest's intrastate toll rates must be above the sum of access charges and toll costs. [40]/ Finally, both Qwest's intrastate access charges and its intrastate long distance rates must be, and have been, approved by the Montana PSC, which presumably knows how to enforce its own rules and has done so. [41]/

B. The Opposing Parties' Price Squeeze Allegations Are Even Less Convincing Than in the Prior Qwest 271 Proceedings, In Which Qwest Thoroughly Refuted Them.

23. Given Qwest's recent UNE rate reductions, [42]/ the price squeeze allegations raised once again by AT&T and other parties have even less merit than in the preceding applications. [43]/ Qwest has previously demonstrated that there is no price squeeze between retail rates and UNE-P or resale rates in any of the

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[39]/ *See Hays Letter.*

[40]/ *Qwest II* Montana Consumer Counsel Reply Comments at 4-5.

[41]/ *Id.* at 3.

[42]/ *Qwest Oct. 7 Ex Parte.*

[43]/ AT&T *Qwest III* Comments Brief at 78-81; AT&T *Qwest III* Lieberman/Pitkin Decl. at ¶¶ 21-48; OneEighty *Qwest III* Comments at 5-6; WorldCom *Qwest III* Comments Attachment A. *Compare Qwest I* Thompson Reply Decl., ¶¶ 121-46; *Qwest II* Thompson Reply Decl., ¶¶ 68-100.

applicant states, and no party here has presented any new evidence to the contrary. WorldCom merely incorporates by reference its *Qwest I* and *Qwest II* filings alleging a price squeeze. AT&T reasserts a price squeeze in Iowa, Idaho, Montana, and Washington – apparently abandoning its previous allegations of a UNE price squeeze in North Dakota, Utah and Wyoming.[44] For each of the four remaining states, AT&T here presents cost and revenue figures different from those it presented in its *Qwest I* and *Qwest II* filings. In each case, AT&T now concedes a *higher* gross margin than it admitted before.[45] As I have explained previously, AT&T has failed utterly to substantiate its asserted cost and revenue figures, which remain subject to the numerous flaws explained at length in Jerrold Thompson's *Qwest I* and *Qwest II* declarations.[46]

24. AT&T claims that the Commission is bound to accept AT&T's own internal cost "estimates" because "Qwest has *not* submitted any evidence that

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[44] *See* AT&T *Qwest I* Comments at 137-41; AT&T *Qwest II* Comments at 96, 155.

[45] In its *Qwest I* and *Qwest II* filings, AT&T claimed that the monthly per-line statewide average residential margins available in Iowa, Idaho, Montana and Washington equaled $4.24, $5.55, $4.26, and $6.09, respectively. In this proceeding, AT&T acknowledges higher margins, equaling $5.38, $6.52, $6.28, and $6.76, respectively. AT&T *Qwest III* Lieberman/Pitkin Decl., ¶ 46; *Ex Parte* Letter from Christopher T. Shenk, Attorney for AT&T Corp., to Marlene H. Dortch, Secretary, FCC, WC Docket No. 02-314 (Oct. 22, 2002).

[46] In addition to its erroneous claim that UNE costs exceed available revenues, AT&T also asserts that "local entry in Wyoming and Montana also is foreclosed by Qwest's anticompetitive deaveraging methodology." AT&T *Qwest III* Comments at 79 n.280. As Qwest explained at length in its *Qwest II* filings, the deaveraging approach adopted by the Wyoming and Montana commissions is TELRIC-compliant. *See Qwest II* Thompson Reply Decl. ¶¶ 44-54.

contradicts" those estimates. AT&T at 79 That assertion is not only baseless, but highly ironic in light of the fact that AT&T did not even present its estimates to state commissions for their review, as required in Section 271 proceedings. In all events, AT&T's assertion (1) distorts the parties' respective burdens in the section 271 context; (2) neglects the fact that the Commission has already repudiated the very evidence AT&T demands that it credit here; and (3) is simply false as a factual matter, given that Qwest has presented the most relevant evidence available to refute AT&T's figures.

25. First, as I have demonstrated in my previous declarations, the Colorado Hearing Commissioner, the Multistate Facilitator and the Utah Public Utility Commission Staff each found that AT&T had failed to present a viable price squeeze analysis, and AT&T failed entirely to address this criticisms in its filings before the various other state commissions. [47]/ Here, too, AT&T fails to recognize that *it* – not *Qwest* – bears the burden of proof in demonstrating a price squeeze. AT&T has failed completely to carry this burden.

26. The FCC's orders make clear that parties alleging a price squeeze, just like parties alleging any other "unusual circumstance" as part of the public interest inquiry, bear the burden of proof.[48] Accordingly, the FCC has *never*

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[47]/ *See Qwest I* Thompson Reply Decl. ¶ 121; *Qwest II* Thompson Reply Decl. ¶ 68.

[48] If the applicant were required to bear the burden of disproving an unusual circumstance, it "would be in the untenable position of having to prove a negative (that is, of coming up with, and rebutting, arguments why its application might not satisfy the requirements of section 271)." *Ameritech Michigan Order* at ¶ 44 n. 86.

required the carrier applying for long-distance authority to *disprove* the existence of a price squeeze, but instead has consistently evaluated only the evidence and the arguments raised by parties *opposing* long-distance authority. [49]/ Indeed, as the Commission has made clear, parties opposing approval must present evidence regarding not only their UNE costs and basic revenues, but also their "ability … to leverage their presence in the long-distance or business markets . . . into an economically viable residential telephone service business,"[50] "revenue from services other than traditional voice services," "revenues from federal universal service funds" and "revenues from business lines." [51]/

27. Second, the Commission has already rejected the *very same evidence* that AT&T claims it is now bound to credit. AT&T relies on affidavits submitted by Mr. Bickley during the *Qwest I* and *Qwest II* applications purportedly demonstrating its internal costs. [52]/ But as the Commission determined in its

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See generally Kansas/Oklahoma 271 Order at ¶ 281; *Vermont 271 Order* at ¶ 61; *New Jersey271 Order* at ¶ 166; *Georgia/Louisiana 271 Order* at ¶ 280 (considering whether the *commenters* have adduced sufficient proof of their claims of "unusual circumstances," not whether the BOC has adequately disproved the commenters' allegations.).

[49]/ *See, e.g.*, *Verizon New Jersey Order* at ¶ 175 ("[W]e reject commenters' allegations of a price squeeze and conclude that there is no evidence in the record that warrants disapproval of this application based on such contentions."); *Verizon Vermont Order* at ¶ 73 (same); *BellSouth Georgia/Louisiana Order* at ¶ 290 (same); *Verizon Delaware/New Hampshire Order* at ¶ 145 (same).

[50]/ *Verizon Vermont Order* at ¶ 71.

[51]/ BellSouth Five-State 271 Order, ¶ 282.

[52]/ AT&T *Qwest II* Bickley Decl.

BellSouth Five-State Order, Mr. Bickley's testimony provides no "cost or other data" supporting the cost figures presented, and no reason to believe that those figures "represent [the costs] of an 'efficient competitor.'" 53/ The same is true of the virtually identical Bickley declarations AT&T has submitted here, as explained previously. 54/

28. Third, AT&T's claims to the contrary notwithstanding, Qwest *has* presented the most reliable and relevant evidence available regarding the costs of efficient provision of retail service: the resale "avoided costs" established by each relevant state commission in the context of proceedings designed precisely to determine the internal "marketing, billing, collection, and other costs" associated with retail. 55/ These costs are, in each case, far below the costs claimed by AT&T.

IV. QWEST COMPLIES WITH CHECKLIST ITEM 1, AND THE COMMISSION SHOULD DISMISS LEVEL 3'S ARGUMENT THAT INTERNET-BOUND TRAFFIC SHOULD COUNT AS "LOCAL" IN THE PRICING OF INTERCONNECTION TRUNKS

29. The Commission should pay no heed to Level 3's complaint that Qwest does not count Internet-bound traffic when determining the relative use of the two-way facilities carrying local and Internet-bound traffic on Qwest's side of the point of interface. The Commission has held numerous times that disputes over

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53/ *See BellSouth Five-State Order* at ¶ 288.

54/ *See Qwest I* Thompson Reply Decl. at ¶¶ 130-39; *Qwest II* Thompson Reply Decl. at ¶¶ 85-94.

55/ *See Qwest I* Thompson Reply Decl. at ¶ 137; *Qwest II* Thompson Reply Decl. at ¶ 92; *Local Competition Order*, 11 FCC Rcd at 15955, ¶ 908.

the regulatory treatment of Internet-bound traffic will not be addressed in the context of Section 271 proceedings. [56/] This issue has no place in a section 271 proceeding, because the traffic on which the dispute is focused – dial-up traffic that originates with an ILEC end user and proceeds via a CLEC to an Internet service provider, which then interconnects it with the world-wide Internet network [57/] – is not subject to Sections 251 or 252 at all. [58/] This ruling remains in effect; although the rationale for it is to be re-examined pursuant to the D.C. Circuit's remand decision, neither the *ISP Reciprocal Compensation Order* nor the rules promulgated in that order have been vacated. [59/]

56/ *See, e.g., Georgia/Louisiana 271 Order* at ¶ 272; *Pennsylvania 271 Order*, 16 FCC Rcd at 17484, ¶ 119.

57/ Qwest delivers this traffic to the CLEC over two-way interconnection facilities that extend from the originating Qwest end office switch to the CLEC switch. These Qwest-provided two-way facilities are priced at TELRIC to the CLEC, but the price for the service is reduced to reflect the relative use of the facility by Qwest. Level 3 presents an extreme case in that it originates no traffic whatsoever. Thus, Level 3's position would have Qwest provide facilities at no charge to Level 3 so that Level 3 and its Internet service provider customers may benefit.

58/ *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Intercarrier Compensation for ISP-Bound Traffic*, Declaratory Ruling in CC Docket No. 96-98 and Notice of Proposed Rulemaking in CC Docket No. 99-68, 14 FCC Rcd 3689 (1999), *remanded sub nom. Bell Atlantic Tel. Cos. v. FCC*, 206 F.3d 1 (D.C. Cir. 2000); *Intercarrier Compensation for ISP-Bound Traffic*, 16 FCC Rcd 9151 (2001) ("*ISP Intercarrier Compensation Order*"), *remanded sub nom. WorldCom, Inc. v. FCC*, 288 F.3d 429(D.C. Cir. 2002).

59/ Although the United States Court of Appeals for the District of Columbia Circuit recently remanded the *ISP Intercarrier Compensation Order*, the court did not vacate that order or the relevant rules. *See WorldCom, Inc. v. FCC*, 288 F.3d at 434. Moreover, the court's opinion addressed only the Commission's treatment of "the compensation between two LECs involved in delivering Internet-bound traffic

30. In any event, Level 3's position is also wrong. The FCC rule relating to "relative use," 47 C.F.R. § 51.709(b), establishes that Internet traffic should be excluded from the relative use calculations that interconnecting carriers use to determine Qwest's proportionate financial responsibility for their interconnection trunks. Under this rule, carriers allocate financial responsibility for the interconnection trunks connecting their networks based on the amount of "traffic" each carrier originates over the trunks. The "traffic" referred to in this rule expressly excludes "interstate or intrastate exchange access." [60/] Because Internet traffic is interstate access, [61/] it is excluded from the traffic used to determine carriers' relative use of interconnection trunks.

31. Finally, it is clear from Level 3's filing that Level 3 is mounting a collateral attack on an issue that it has already lost in arbitration before the Colorado and Oregon PUCs, and that it is now challenging before the U.S. District

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to an ISP;" the court did not address, let alone remand or vacate, Section 51.701 of the Commission's rules. *Id* at 431.

60/ *See* 47 C.F.R. § 51.701(b)(1). *See also Local Competition Order*, 11 FCC Rcd at 15598, ¶ 191 (interexchange traffic is not considered "telephone exchange or exchange access," and therefore interconnection trunks carrying interexchange or interstate traffic are not eligible for Section 251(c)(2) treatment), *aff'd in pertinent part sub nom. Competitive Tel. Ass'n v. FCC*, 117 F.3d 1068 (8th Cir. 1997); *subsequent history omitted*. Applying an end-to-end analysis, the FCC concluded that calls to ISPs do not terminate at the ISP's local server, but instead continue to the ultimate destination or destinations. Moreover, the FCC has previously held that state regulators have authority to determine whether calls passing between LECs should be subject to reciprocal compensation for those areas where the LECs' service areas do not overlap. *Local Competition Order*, 11 FCC Rcd at 16013, ¶ 1035.

61/ *ISP Intercarrier Compensation Order, 16 FCC Rcd at* ¶¶ 52, 57.

Courts for the District of Colorado and the District of Oregon. [62]/ To the extent that Level 3 believes that the existing regime creates improper incentives, is economically inefficient, or adversely affects competition, it should advocate alternative payment regimes before the Commission in the pending *Intercarrier Compensation* rulemaking docket [63]/ and not in the context of this Section 271 proceeding.

V. CONCLUSION

32. The information in our initial and reply Declarations in WC Docket Nos. 02-148 and 02-189, and in this Reply Declaration, provides ample basis for the FCC to conclude that Qwest's rates for UNEs, collocation, and other interconnection elements in Colorado, Idaho, Iowa, Montana, Nebraska, North Dakota, Utah, Wyoming, and Washington are just, reasonable, consistent with the FCC's TELRIC methodology, and within the range that a reasonable application of TELRIC principles would produce.

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[62]/ *See* Level 3 *Qwest III* Comments at 7 n.9 and Attachment B (referring to judicial proceedings).

[63]/ *Developing a Unified Intercarrier Compensation Regime*, Notice of Proposed Rulemaking, 16 FCC Rcd 9610 (2001). *See also ISP Intercarrier Compensation Order*, 16 FCC Rcd at ¶ 76 footnote 145, "A number of questions must be resolved before we are prepared to implement fully a bill and keep regime where most costs are recovered from end-users. (We say most, not all, costs are recovered from end-users because a bill and keep regime may include intercarrier charges for transport between networks.) These questions include, for example, the allocation of transport costs between interconnecting carriers and the effect on retail prices of adopting a bill and keep regime that is not limited to ISP-bound traffic. We seek comment on these and other issues in the accompanying *Intercarrier NPRM."*

33. This concludes our declaration.